

General Information Letter: Petition for alternative apportionment cannot be granted based on unsupported assertion that the statutory apportionment formula fails to properly apportion income.

January 27, 2003

Dear:

This is in response to your letter dated December 19, 2002 in which you request permission to use an alternative method of allocation or apportionment. Department of Revenue ("Department") regulations require that the Department issue only two types of letter rulings, Private Letter Rulings ("PLRs") and General Information Letters ("GILs"). PLRs are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding against the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. GILs do not constitute statements of Department policy that apply, interpret or prescribe the tax laws and are not binding against the Department. See 2 Ill. Adm. Code 100.1200(b) and (c).

Although a ruling granting an alternative allocation or apportionment has been requested, because the petition fails to sustain the burden of proof required pursuant to 86 Ill. Adm. Code 100.3390 the Department must respond by GIL denying the petition.

In your letter you have stated as follows:

COMPANY ("the Company") is a designer, developer and supplier of host bus adapters. Beginning in our tax year ending July 1, 2001, the Company began doing business with a contract manufacturer located in Illinois. This entity manufactures and ships certain inventory on behalf of COMPANY.

Prior to the beginning of our relationship with the contract manufacturer, COMPANY did not have nexus with the state. However, once we commenced doing business with the contract manufacturer, Company-owned equipment was placed into service at the contract manufacturer's facility. Likewise, certain inventory of COMPANY was also at the location of the contract manufacturer. Thus, the Company filed an initial return with Illinois for the year ending July 1, 2001.

The extended due date of our Illinois return for the fiscal year ending June 30, 2002 is April 15, 2003. Based upon the standard business income apportionment formula, dividing sales attributable to Illinois by sales everywhere, the Company expects to have an apportionment factor of approximately 9.0%. The Company feels that the standard business income apportionment formula does not accurately and fairly reflect our business activity in the state. We feel this way because the Company has:

- ? No employees, offices or other places of business in Illinois (our payroll factor is 0%).
- ? Minimal property in the state (our Illinois property factor is approximately 3.0%).
- ? Total sales to Illinois customers, excluding throwback sales, that are less than 1.9% of total sales everywhere (inclusion of throwback sales raises the standard business income apportionment formula to approximately 9.0%).

Using a three-factor apportionment formula, evenly weighting sales, property and payroll, we expect that our Illinois apportionment factor would be approximately 55%-60% less than the apportionment factor computed using the standard business income apportionment formula.

Given the above information, we respectfully request that we receive consideration for an alternative apportionment formula, as provided for in Illinois Income Tax Regulations Section 100.3390. Specifically, we would like to request permission to use a three-factor formula in which sales, property, and payroll are equally weighted (1/3 sales, 1/3 property and 1/3 payroll). If granted, this apportionment formula would be applicable beginning with our fiscal year ending June 30, 2002.

RULING

Illinois Income Tax Regulations Section 100.3390 (86 Ill. Adm. Code 100.3390) allows a taxpayer to petition the Department for use of an alternative apportionment formula where the allocation and apportionment provisions of IITA Section 304(a) through (e) do not fairly represent the extent of the taxpayer's business activity in Illinois.

Regulations Section 100.3390(c) sets forth a taxpayer's burden of proof.

Burden of Proof. A departure from the required apportionment method is allowed only where such methods do not accurately and fairly reflect business activity in Illinois. An alternative apportionment method may not be invoked, either by the Director or by a taxpayer, merely because it reaches a different apportionment percentage than the required statutory formula. However, if the application of the statutory formula will lead to a grossly distorted result in a particular case, a fair and accurate alternative method is appropriate. The party (the Director or the taxpayer) seeking to utilize an alternative apportionment method has the burden [of] going forward with the evidence and proving by clear and cogent evidence that the statutory formula results in the taxation of extraterritorial values and operates unreasonably and arbitrarily in attributing to Illinois a percentage of income which is out of all proportion to the business transacted in the State. In addition, the party seeking to use an alternative apportionment formula must go forward with the evidence and prove that the proposed alternative apportionment method fairly and accurately apportions income to Illinois based upon business activity in this State.

In addition, Regulations Section 100.3390(d) states:

A petition will be summarily rejected if its sole basis for support rests on the fact that an alternative method reaches a different apportionment percentage than the required statutory formula.

In this case, the petition contains as its sole basis for support the fact that an evenly weighted three-factor formula consisting of property, payroll, and sales reaches a different apportionment percentage than the required statutory formula. The petition states that the statutory formula does not fairly reflect the extent of the taxpayer's business activities in Illinois because the formula does not take into account the taxpayer's payroll and property factors, and applies a throwback rule in determining the

sales factor. The petition states that using instead an evenly weighted three-factor formula is expected to result in a smaller Illinois apportionment factor. Consequently, the petition must be summarily rejected pursuant to Regulations Section 100.3390(d).

As stated above, this is a GIL. A GIL does not constitute a statement of policy that applies, interprets or prescribes the tax laws, and it is not binding on the Department. If you wish to obtain a PLR which will bind the Department, please submit a request conforming to the requirements of 2 Ill. Adm. Code 100.1200 and 86 Ill. Adm. Code 100.3390.

Sincerely,

Brian L. Stocker
Associate Counsel (Income Tax)